

COMPANY UPDATE

ASUSTeK Computer (2357.TW)

Sell

Garmin-ASUS alliance unlikely to create waves in 2009**What's changed**

Garmin and ASUSTeK held a joint press conference on their strategic alliance. Key takeaways: 1) ASUSTeK/Garmin going forward will co-brand all phone-based products as "Garmin Asus"; 2) Garmin-ASUS products will feature fine integration of handset/GPS/LBS functions with a more user-friendly interface and better usability; 3) Garmin/ASUS will introduce their first new smartphone product in mid-Feb at Barcelona 3GSM but the ramp-up of a more complete product lineup may not occur until 2010. No further details of the alliance were provided due to confidentiality agreements.

Implications

Though we see some synergy in the alliance (e.g., Garmin's distribution channel, brand franchise, strong GPS software interface; ASUS' experience in the smartphone market and R&D capability) and believe co-branding should be positive for ASUSTeK's handset business, we think it is too early to draw conclusions as to how the alliance may benefit ASUS. Our key concerns include: 1) the value proposition of such GPS phones to attract a broad base of consumers; 2) Garmin's lack of experience and ASUS' decade-long efforts to break into the handset market; 3) the already crowded smartphone market and high hurdle for newcomers to make a meaningful breakthrough. We maintain our estimates on ASUSTeK.

Valuation

We maintain SOTP-based 12m NT\$25 TP and Sell rating (Conviction list).

Key risks

Faster-than-expected macro recovery and netbook market share gain.

Impact on related securities

We believe the alliance should have a limited impact on MiTAC (2315.TW, Sell) given MiTAC's low exposure to the GPS-phone sector; as for Garmin (GRMN, Sell (Conv List)), we remain skeptical of its entry into the smartphone market given increasing competition in an already competitive market.

INVESTMENT LIST MEMBERSHIP

Asia Pacific Sell List

Asia Pacific Conviction Sell List

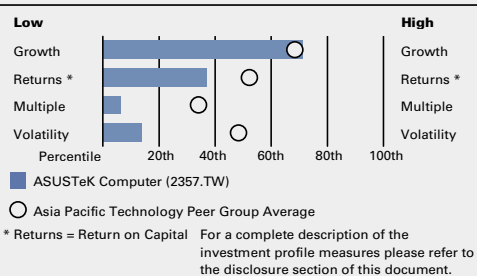
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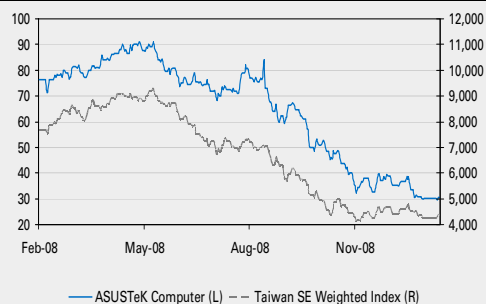
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Investment Profile

Key data	Current
Price (NT\$)	30.50
12 month price target (NT\$)	25.00
Market cap (NT\$ mn / US\$ mn)	129,504.6 / 3,842.6
Foreign ownership (%)	24.9

	12/07	12/08E	12/09E	12/10E
EPS (NT\$)	6.84	3.87	2.48	3.58
EPS growth (%)	39.7	(43.4)	(36.0)	44.4
EPS (diluted) (NT\$)	6.76	3.87	2.48	3.58
EPS (basic pre-ex) (NT\$)	6.84	3.87	2.48	3.58
P/E (X)	4.5	7.9	12.3	8.5
P/B (X)	0.8	0.7	0.7	0.7
EV/EBITDA (X)	8.0	2.8	1.9	1.8
Dividend yield (%)	7.4	3.2	2.1	3.2
ROE (%)	18.8	9.7	5.9	8.1

Price performance chart

Share price performance (%)	3 month	6 month	12 month
Absolute	(37.0)	(57.0)	(60.0)
Rel. to Taiwan SE Weighted Index	(28.3)	(31.7)	(30.1)

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 2/04/2009 close.

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ASUSTeK Computer: Summary financials

Profit model (NT\$ mn)	12/07	12/08E	12/09E	12/10E	Balance sheet (NT\$ mn)	12/07	12/08E	12/09E	12/10E
Total revenue	755,360.7	766,671.2	651,670.8	692,226.9	Cash & equivalents	43,585.8	72,688.9	97,633.2	88,530.5
Cost of goods sold	(680,591.8)	(681,919.2)	(587,337.1)	(623,502.6)	Accounts receivable	129,134.5	58,931.7	49,865.7	64,470.1
SG&A	(36,995.8)	(58,191.5)	(45,692.7)	(43,160.2)	Inventory	103,423.8	85,320.9	62,129.7	95,989.0
R&D	(9,102.2)	(12,273.0)	(7,971.0)	(8,253.7)	Other current assets	25,590.2	28,603.0	27,561.8	28,145.3
Other operating profit/(expense)	0.0	0.0	0.0	0.0	Total current assets	301,734.2	245,544.5	237,190.4	277,135.0
ESO expense	--	--	--	--	Net PP&E	63,176.7	66,493.0	65,968.4	64,137.7
EBITDA	36,780.0	23,307.5	20,617.8	28,012.5	Net intangibles	1,986.8	2,473.1	2,473.1	2,473.1
Depreciation & amortization	(8,109.1)	(9,020.1)	(9,947.8)	(10,702.2)	Total investments	0.0	0.0	0.0	0.0
EBIT	28,670.9	14,287.4	10,670.0	17,310.3	Other long-term assets	6,645.3	6,504.4	6,504.4	6,504.4
Interest income	1,636.0	1,050.0	1,040.0	1,250.0	Total assets	385,742.0	332,868.7	323,990.0	362,103.8
Interest expense	(804.1)	(557.1)	(519.1)	(477.7)	Accounts payable	141,564.9	81,712.3	70,330.7	97,213.9
Income/(loss) from uncons. subs.	422.9	483.1	0.0	0.0	Short-term debt	7,165.9	7,165.9	7,165.9	7,165.9
Others	8,658.3	6,859.5	3,550.0	3,400.0	Other current liabilities	37,263.4	32,926.9	29,669.6	28,990.8
Pretax profits	38,584.1	22,122.9	14,740.9	21,482.7	Total current liabilities	185,994.3	121,805.1	107,166.2	133,370.7
Income tax	(7,828.4)	(4,377.0)	(2,727.9)	(4,138.8)	Long-term debt	16,389.0	17,061.7	17,061.7	17,061.7
Minorities	(3,132.4)	(1,647.7)	(1,707.6)	(2,465.4)	Other long-term liabilities	22,409.5	22,409.5	22,409.5	22,409.5
Net income pre-preferred dividends	27,623.3	16,098.2	10,305.4	14,878.5	Total long-term liabilities	38,798.5	39,471.2	39,471.2	39,471.2
Preferred dividends	0.0	0.0	0.0	0.0	Total liabilities	224,792.8	161,276.3	146,637.4	172,841.9
Net income (pre-exceptionals)	27,623.3	16,098.2	10,305.4	14,878.5	Preferred shares	0.0	0.0	0.0	0.0
Post-tax exceptionals	0.0	0.0	0.0	0.0	Total common equity	160,949.2	171,592.4	177,352.6	189,262.0
Net income	27,623.3	16,098.2	10,305.4	14,878.5	Minority interest	0.0	0.0	0.0	0.0
EPS (basic, pre-except) (NT\$)	6.84	3.87	2.48	3.58	Total liabilities & equity	385,742.0	332,868.7	323,990.0	362,103.8
EPS (basic, post-except) (NT\$)	6.84	3.87	2.48	3.58	BVPS (NT\$)	39.83	41.27	42.66	45.52
EPS (diluted, post-except) (NT\$)	6.76	3.87	2.48	3.58					
EPS excl. ESO expense (basic) (NT\$)	6.84	4.19	2.57	3.74					
EPS excl. ESO expense (dil.) (NT\$)	6.76	4.19	2.57	3.74					
DPS (NT\$)	2.26	0.97	0.64	0.97					
Dividend payout ratio (%)	33.1	25.0	26.0	27.0					
Free cash flow yield (%)	4.4	24.7	25.0	(2.9)					
Growth & margins (%)	12/07	12/08E	12/09E	12/10E	Ratios	12/07	12/08E	12/09E	12/10E
Sales growth	34.8	1.5	(15.0)	6.2	ROE (%)	18.8	9.7	5.9	8.1
EBITDA growth	40.0	(36.6)	(11.5)	35.9	ROA (%)	7.4	4.5	3.1	4.3
EBIT growth	40.9	(50.2)	(25.3)	62.2	ROACE (%)	23.5	13.1	10.2	14.6
Net income growth	43.7	(41.7)	(36.0)	44.4	Inventory days	57.3	50.5	45.8	46.3
EPS growth	39.7	(43.4)	(36.0)	44.4	Receivables days	63.2	44.8	30.5	30.1
Gross margin	9.9	11.1	9.9	9.9	Payable days	82.7	59.8	47.2	49.0
EBITDA margin	4.9	3.0	3.2	4.0	Net debt/equity (%)	(20.4)	(36.1)	(49.0)	(41.1)
EBIT margin	3.8	1.9	1.6	2.5	Interest cover - EBIT (X)	NM	NM	NM	NM
					Valuation	12/07	12/08E	12/09E	12/10E
Cash flow statement (NT\$ mn)	12/07	12/08E	12/09E	12/10E	P/E (analyst) (X)	4.5	7.9	12.3	8.5
Net income pre-preferred dividends	27,623.3	16,098.2	10,305.4	14,878.5	P/B (X)	0.8	0.7	0.7	0.7
D&A add-back	8,109.1	9,020.1	9,947.8	10,702.2	EV/EBITDA (X)	8.0	2.8	1.9	1.8
Minorities interests add-back	0.0	0.0	0.0	0.0	Dividend yield (%)	7.4	3.2	2.1	3.2
Net (inc)/dec working capital	(15,373.2)	28,453.1	20,875.6	(21,580.6)					
Other operating cash flow	11,571.8	(10,791.7)	(2,216.1)	(1,262.2)					
Cash flow from operations	28,405.1	41,432.3	38,912.6	2,737.9					
Capital expenditures	(14,868.5)	(10,503.4)	(7,590.0)	(7,038.4)					
Acquisitions	0.0	(1,375.4)	0.0	0.0					
Divestitures	0.0	0.0	0.0	0.0					
Others	(2,941.9)	(1,192.3)	(1,683.1)	(1,683.1)					
Cash flow from investments	(17,810.4)	(13,071.1)	(9,273.2)	(8,721.5)					
Dividends paid (common & pref)	(6,244.5)	(9,146.5)	(4,024.5)	(2,679.4)					
Inc/(dec) in debt	818.6	(6.3)	0.0	0.0					
Common stock issuance (repurchase)	3,049.3	308.5	0.0	0.0					
Other financing cash flows	838.0	9,589.9	(670.7)	(439.7)					
Cash flow from financing	(1,538.5)	745.6	(4,695.2)	(3,119.0)					
Total cash flow	8,894.4	29,103.2	24,944.3	(9,102.7)					

Note: Last actual year may include reported and estimated data.
Source: Company data, Goldman Sachs Research estimates.

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Garmin and ASUSTeK to form brand alliance for phone products

Garmin (GRMN) and ASUSTeK (2357.TW) held a joint press conference on 2/4, to announce their strategic alliance. Key takeaways: (1) ASUSTeK and Garmin going forward will co-brand all phone-based products as "Garmin-ASUS"; (2) ASUSTeK has become a branding partner for Garmin from originally only an ODM supplier through Pegatron for Garmin's nüvifone; (3) the Garmin-ASUS new products will feature integration of handset/GPS/LBS functions with more user-friendly interface and better usability; (4) Garmin-Asus will introduce its first new smartphone product in mid-Feb at Barcelona 3GSM and the model will be based on Garmin's nüvifone G60 model; (5) the two companies expect to ramp up a more complete product lineup in 2010. No further details of the alliance (e.g., form of alliance, profit sharing, etc.) were provided due to confidentiality agreements.

Our industry sources suggest that the first Garmin-ASUS smartphone should launch in the US market first in 2Q09, applying Garmin's operating system and interface based on Linux. The selling price is likely to lie between US\$500 to US\$700 (without contract). The company plans to launch 3-4 smartphone models in 2009.

Some synergies expected, but lots of obstacles to overcome

We see some synergies from this co-branding alliance. In our view, ASUSTeK may leverage Garmin's distribution channel, brand franchise in the dedicated PND (portable navigation device) segment and software capability in GPS interface; Garmin may make a tangible breakthrough in the GPS-capable smartphone segment through ASUSTeK's experience in the handset market.

Although we think co-branding should be positive for ASUSTeK's handset business, we believe it is too early to draw conclusions as to how it might contribute to ASUSTeK for the following reasons:

- (1) GPS is not the major application of a smartphone though many smartphone models have embedded GPS or AGPS features, so GPS may not be the key factor, only a nice-to-have feature, when potential buyers consider the smartphone;
- (2) ASUSTeK handset has not yet reached economies of scale after almost ten years since the business was started in 1999. On the other hand, time-to-market and execution of Garmin's GPS-phone product rampup is questionable, evident by delayed commercial shipments of its nüvifone product (introduced more than a year ago in January 2008 although it has not yet hit the shelves);
- (3) Though it is arguable whether Garmin's nüvifone G60 model has more advanced LBS functionality than other smartphones in the market, we do not think the entry barrier for such an LBS-capable GPS phone is high and believe competitors may easily catch up. In fact, Nokia is already ahead of Garmin on built-in LBS function with its N-series smartphones;
- (4) Despite high exposure to notebook/motherboard, and PND markets, respectively, neither Garmin nor ASUSTeK has a solid enough presence in the smartphone space; and
- (5) We think the smartphone market is already crowded enough, being currently dominated by industry leaders such as Nokia, Apple, Samsung, HTC, Palm, RIMM, etc., with Dell and Acer entering the market this year.

- (6) Handheld business shipments for ASUSTeK reached only several hundred units in 2008 and the revenue contribution accounted for a low single digit percentage of ASUSTeK's total sales.

Implications for Garmin and MiTAC

In regards to Garmin (GRMN, covered by Thomas Lee), this announcement does not change our investment view on the stock (Sell, Conviction List) as we remain skeptical of Garmin's entry into the smartphone market given increasing competition in an already competitive market. In addition to Apple, RIM, and HTC, which all have compelling GPS-enabled smartphones in the marketplace, we expect a greater push from other established handset vendors such as Nokia (acquired map supplier, NAVTEQ), Samsung and LG. Considering that the US market is an operator driven market that depends highly on handset subsidies to drive sales, we believe Garmin may have a difficult time making any meaningful inroads over the foreseeable future given the high barriers of entry in the US handset market. As a result, we believe Garmin's move into the mobile handset market carries significant risk.

In regards to MiTAC International (2315.TW, Sell, covered by Matthew Chuang), we do not expect the alliance to bring much impact to MiTAC at least for the short-to-mid term, as GPS phone is not MiTAC's focus area. That said, we think the announcement is one more signal that the addressable market for dedicated PNDs may get further squeezed by convergence smartphones with embedded GPS functions. Meanwhile, we continue to see limited room for MiTAC as a distant no. 3 vendor to compete against industry leaders in the current market environment given the weak macro outlook and more cautious consumer spending patterns.

Reg AC

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Growth is a composite of next year's estimate over current year's estimate, e.g. EPS, EBITDA, Revenue. **Return** is a year one prospective aggregate of various return on capital measures, e.g. CROCI, ROACE, and ROE. **Multiple** is a composite of one-year forward valuation ratios, e.g. P/E, dividend yield, EV/FCF, EV/EBITDA, EV/DACF, Price/Book. **Volatility** is measured as trailing twelve-month volatility adjusted for dividends.

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There are no company-specific disclosures for: MiTAC International (NT\$11.10)

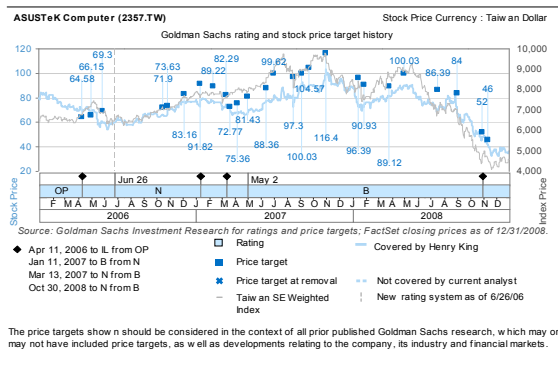
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Price target and rating history chart(s)



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Definitions

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Coverage views: Attractive (A). The investment outlook over the following 12 months is favorable relative to the coverage group's historical fundamentals and/or valuation. **Neutral (N).** The investment outlook over the following 12 months is neutral relative to the coverage group's historical fundamentals and/or valuation. **Cautious (C).** The investment outlook over the following 12 months is unfavorable relative to the coverage group's historical fundamentals and/or valuation.

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